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OWNERSHIP OF INTERESTS IN OIL AND GAS

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Since Col. Drake drilled the first well in 1859, courts and lawyers have been preoccupied with attempts to define the character of the ownership of oil and gas in place. There are a number of excellent articles and treatises which explore at length the divergent views that have been developed. This paper may nevertheless be justified if it does no more than serve as a guide to more exhaustive treatments of the subject.

The courts have had difficulty in formulating a meaningful theory of ownership of oil and gas. Some trouble arises from the lack of a satisfactory analogy between these fluids and other substances with judicially determined property characteristics. Another significant reason has been the universal adoption of a doctrine which writers and courts have lately called the Rule of Capture.

EARLY OBSERVATIONS UPON THE NATURE OF UNEXTRACTED OIL AND GAS

Employing the traditional common-law process of reasoning, the courts sought in vain for the perfect analogy for oil and gas when they were newly discovered substances. Because of limited and frequently inaccurate knowledge about the occurrence of oil and gas, and the movement of these fluids beneath the earth's surface, the comparisons made in some of the earlier cases now seem whimsical. Sometimes oil and gas were compared to underground percolating water.[1] The analogy was unsound, however, because the movement of oil and gas is influenced almost entirely by pressure rather than gravity, which is usually the primary force responsible for the movement of percolating waters. There is a difference in value and in frequency of occurrence which further distinguishes oil and gas. Normally, the supply of water is constantly being replenished, which is not true of oil and gas. Still less apt was the comparison made to wild animals. According to some notions oil and gas wandered about aimlessly in subterranean channels. A Kentucky court referred to the "wild and migratory nature of oil and gas,"

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1 Peoples Gas Co. v. Tyner, 131 Ind. 277, 31 N.E. 59 (1892); Dark v. Johnston, 55 Pa. 164 (1867).

and stated: "They may be here today and gone tomorrow." [2] A Texas court said that oil and gas are supposed to "percolate restlessly about under the surface of the earth, even as the birds fly from field to field and the beasts roam from forest to forest. . . ." [3] Another statement frequently quoted is: "Water and oil, and still more strongly gas, may be classed by themselves, if the analogy be not too fanciful, as minerals *ferae naturae*." [4]

One of the interesting early cases is *Wood County Petroleum Co. v. West Virginia Transp. Co.*[5] The assignee of a lease for the sole purpose of mining for "rock or carbon oil" drilled a well which produced small quantities of oil but a large amount of gas. Some of this gas was used or sold off the premises and the lessors sued to recover the value of the gas. The court concluded that the lessee was entitled to appropriate the gas without compensation to the lessor since it came to the surface of its own force as a necessary incident to the production of the oil. The court compared the gas to percolating water and to air. It took note of the fact that the "eternal fires" of Baku on the Caspian Sea, had been burning for ages. The court noted that the first gas well near East Liverpool, Ohio was opened in 1859 and at the time of the opinion neither it nor any of those subsequently drilled showed any sign of failing. Thus the court was of the opinion—although it admitted exact knowledge did not exist —that the supply of gas was inexhaustible and without limit. It thus concluded that natural gas "partakes more nearly of the character of the elements air and water than it does of those things which are the subject of absolute property." [6] One of the lessor's contentions was that there had been no valid assignment from the original lessee to the defendant, so that the defendant was a trespasser. Although the contention was rejected, the court said: "The fact that the plaintiff [lessor] had the title to and possession of the land would give it the legal right to recover damages from the appellant for any injury done to it by trespassing thereon. But the appropriation of the gas would not enter into the estimate of such damages, because, as we have seen, such appropriation would be regarded as *damnum absque injuria. It would no more be a part of such damages than would the consumption of the air or water by a trespasser upon the premises.*" [7] It would come as no surprise to an

[2] Hammonds v. Central Ky. Natural Gas Co., 255 Ky. 685, 688, 75 S.W.2d 204, 205 (1934).

[3] Medina Oil Dev. Co. v. Murphy, 233 S.W. 333, 335 (Tex. Civ. App. 1921).

[4] Westmoreland Natural Gas Co. v. Dewitt, 130 Pa. 235, 249, 18 Atl. 724, 725 (1889).

[5] 28 W. Va. 210 (1886).

[6] *Id.* at 217.

[7] *Id.* at 220. (Emphasis added.) Insofar as the theory of ownership is concerned,

experienced oil and gas lawyer to learn that the Pennsylvania court reached the same result on similar facts a few years earlier, but took the position that the owner of the land owns absolutely the oil and gas beneath it.[8]

Today it is known that oil and gas are for all practical purposes static in the reservoir until it has been punctured by a well. When drilling occurs, the substances move through the pores of the reservoir rock toward the low pressure area created by the producing well. The movement is quite predictable in terms of both quantity and direction. After a reasonable amount of development has taken place, engineers can determine with fair accuracy the amount of recoverable oil and gas in a reservoir and the amount which can be produced from any given tract, assuming, of course, certain standards of development and operation. In light of this knowledge the analogies to water, air, and wild animals no longer appear in the opinions of the courts.

The Traditional "Remedy" of Self-help

One area of dispute involved in the earlier oil and gas cases was that which arose out of the drainage of one tract by the owner of a neighboring tract. The question whether the adjoining owner was entitled to damages or injunctive relief was squarely presented for the first time in *Kelley v. Ohio Oil Co.*[9] The plaintiff alleged that his neighbor had drilled wells along two of the boundary lines of plaintiff's property, locating them only twenty-five feet from plaintiff's land and unnecessarily close together. It was also alleged that the defendant's act was in violation of the common practice in the industry, which was to drill no closer than two hundred feet from one's property line in order to avoid draining an undue amount of oil from adjacent lands. Plaintiff sought damages and an injunction to prevent future drainage by these operations. The court concluded that plaintiff's only remedy was self-help. It stated:

> While it is generally supposed that oil is drained in the wells for a distance of several hundred feet, the matter is somewhat uncertain, and no right of sufficient weight can be founded upon such uncertain supposition to overcome the well-known right which every man has to use his property as he pleases, so long as he does not interfere with the legal rights of others. Protection of lines of adjoining lands by drilling of wells on both sides of such

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the *Wood County* case was in effect overruled in Williamson v. Jones, 39 W. Va. 231, 19 S.E. 436 (1894).

[8] Kier v. Peterson, 41 Pa. 357 (1861).

[9] 57 Ohio St. 317, 49 N.E. 399 (1897).

> lines affords an ample and sufficient remedy for the supposed grievances complained of in the petition and the supplemental petition, without resort to either an injunction or an accounting.[10]

As stated in another leading case with similar facts, "every landowner or his lessee may locate his wells wherever he pleases, regardless of the interests of others. . . . He may crowd the adjoining farms so as to enable him to draw the oil and gas from them. What then can the neighbors do? Nothing, only go and do likewise." [11] The cases from all jurisdictions have been consistent in denying both legal and equitable relief to an owner of land because of the mere fact of drainage by an adjoining owner.[12] One of the earliest statements of the rule, found in the *Kelley* case, is perhaps as accurate as any that have since been formulated. The court said:

> Whatever gets into the well belongs to the owner of the well no matter where it came from. In such cases the well and its contents belong to the owner or lessee of the land, and no one can tell to a certainty from whence the oil, gas or water which enters the well came, and no legal right as to the same can be established or enforced by an adjoining landowner.[13]

The Rule of Capture: What and Why

Note that the rule as stated by the Ohio court in *Kelly* is simply *nonliability*. An owner of a tract is not accountable to his neighbors for drainage caused by a well legally drilled and bottomed on his own tract, but he has no affirmative right to drain adjoining lands. To claim otherwise begets unfortunate results.[14] The Rule of Capture developed as a matter of necessity. When the early cases

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[10] *Id.* at 328, 49 N.E. at 401.

[11] Barnard v. Monogahela Natural Gas Co., 216 Pa. 362, 365, 65 Atl. 801, 802 (1906).

[12] Occasional dicta to the contrary can be found. Union Gas & Oil Co. v. Fyffe, 219 Ky. 640, 645, 294 S.W. 176, 178 (1927). In Ross v. Damm, 278 Mich. 388, 270 N.W. 722 (1936), an owner of a small tract was awarded damages for conversion by a neighbor who had drilled near the property line. The case however, has been explained as one in which liability was predicated upon the fact that the defendant wrongfully withheld from plaintiff possession of a disputed tract, thus preventing plaintiff from exercising his right of self-help. See generally 1 Kuntz, Oil and Gas § 4.2 (1962).

[13] Kelley v. Ohio Oil Co., *supra* note 9, at 327, 49 N.E. at 401.

[14] See Ryan Consol. Petroleum Corp. v. Pickens, 155 Tex. 221, 285 S.W.2d 201 (1955). See generally Walker, "Property Rights in Oil and Gas and Their Effect Upon Police Regulation of Production," 16 Texas L. Rev. 370 (1938). An excellent discussion of the Rule of Capture is found in Hardwicke, "The Rule of Capture and Its Implications as Applied to Oil and Gas," 13 Texas L. Rev. 391 (1935).

were decided, it was impossible, as stated in the *Kelley* case, to determine the extent to which the production represented drainage from neighboring land. This reason has some validity today, but it has lost much of its force since remarkably accurate estimates can now be made in the early stages of the development of a pool. For another reason, however, it is still a rule of necessity. If *A* and *B* own adjoining tracts, *A* will have little incentive to drill if he must bear all of the risks and be forced to share his production with *B* if it can be proved that some of the oil or gas is drained from *B*'s tract. The rule seems therefore essential if development is to be encouraged.[15]

The impact of the Rule of Capture has been lessened by conservation statutes and regulations adopted under them. The "drill-as-you-please" privilege has been restricted, as has the remedy of self-help in drilling offset wells to protect against drainage. However, it is still applicable to protect against liability when there is no violation of conservation laws, and it, therefore, remains as a rule of fundamental importance.[16]

Property Theories

The writers are by no means consistent in the labels they have selected in order to classify theories of ownership. Williams and Meyers divide the various states into three categories, "ownership-in-place," "non-ownership" and "qualified ownership," but recognize that the latter two are now practically identical.[17] Kulp also divides the states into the same three groups but uses slightly different labels.[18] Sullivan find three categories useful,[19] while Kuntz uses only two, "ownership-in-place" and "exclusive-right-to-take." [20]

Most of the modern authorities are in general agreement that, except for the purpose of categorizing cases having the extreme and now abandoned view of *Wood County Petroleum Co. v. West Virginia Transp. Co.*,[21] only two classifications are necessary to embrace the opposing views as to the nature of the ownership of oil and gas

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[15] Alternatives to the Rule of Capture are explored and rejected in 1 Kuntz, Oil and Gas § 4.1 (1962).

[16] Shank, "Present Status of the Law of Capture," Sixth Annual Institute on Oil and Gas Law and Taxation, Southwestern Legal Foundation 257 (1955).

[17] 1 Williams & Meyers, Oil and Gas Law § 203 (1964).

[18] Kulp, Oil and Gas Rights § 10.5 (1954). (Kulp's three categories are: absolute ownership, non-ownership, and correlative rights.)

[19] Sullivan, Oil and Gas Law § 12 (1955).

[20] 1 Kuntz, Oil and Gas § 2.4 (1962). See 1 Williams & Meyers, *op. cit. supra*, note 17, § 203, for a tabulation of terminology used in law reviews.

[21] See text accompanying note 5 *supra*.

in place. The one which is followed in what appears to be a majority of the producing states is referred to variously as the "ownership-in-place," [22] "absolute ownership," [23] or simply "ownership" theory. Among the labels that have been attached to the opposing theory are "non-ownership-in-place," [24] "non-ownership," [25] "exclusive-right-to-take" [26] and "qualified ownership." [27] The latter term seems the most descriptive, since in all of the states that subscribe to this view it is recognized that the owner of the land in which the reservoir is located has a property interest in the oil and gas in place, and the exclusive right to produce from such land, although he does not have title to it.[28]

The Absolute Ownership Theory

In the ownership states, the owner of the land is regarded as owning the oil and gas beneath it in exactly the same way that he owns coal, iron, or other solid minerals. He can—by a deed granting or excepting the oil and gas in place—effect a severance of them from the surface by a horizontal plane just as he might convey the east half and retain the west half of his tract, making a severance by vertical plane. The concept was expressed in a leading case as follows: "oil and gas in place are minerals and realty subject to ownership, severance and sale while embedded in the sands and rocks beneath the earth's surface in like manner and to the same extent as is coal or any other solid mineral." [29] To the argument that petroleum could be drained away without liability by the owners of neighboring lands, the court replied that the person whose land is drained "has the correlative right to appropriate, through like methods of drainage, the gas and oil underlying the tracts adjacent to his own." [30] The correlative right to compensate for drainage through self-help may not be a logical answer to the argument, but no better one is found in the opinions. Notwithstanding the logical difficulties which flow from the Rule of Capture, it is well settled

22 Hardwicke, *supra* note 14.

23 1 Williams & Meyers, *op. cit. supra* note 17, § 203; Greer, "The Ownership of Petroleum Oil and Natural Gas in Place," 1 Texas L. Rev. 162 (1923).

24 Hardwicke, *supra* note 14.

25 Greer, *supra* note 23.

26 1 Kuntz, Oil and Gas § 2.4 (1962).

27 Walker, *supra* note 14.

28 The absolute ownership view has sometimes been described as one of "qualified property" in view of the fact that the owner may lose his title through the operation of the Rule of Capture. Simonton, "Has a Landowner Any Property in Oil and Gas in Place?" 27 W. Va. L.Q. 281 (1921). See Hardwicke, *supra* note 14.

29 Stephens County v. Mid-Kansas Oil & Gas Co., 113 Tex. 160, 167, 254 S.W. 290, 292 (1923).

30 *Id.* at 167, 254 S.W. at 292.

in the ownership states that the owner of a tract of land, or of a mineral interest severed from it, owns the oil and gas which is in place beneath the tract at any given moment in the same way that he owns the solid minerals.

THE QUALIFIED OWNERSHIP THEORY

The qualified ownership theory is well stated in *Manufacturers' Gas & Oil Co. v. Indiana Natural Gas & Oil Co.*[31] In that case, the defendant used pumps to increase the natural flow of gas from its wells in violation of an Indiana statute. It was shown that the practice would be injurious to the reservoir and the court held that the plaintiffs, who owned other land in the reservoir, were entitled to an injunction to halt the practice. The court noted the differences between natural gas and underground water. In describing the property rights of the plaintiffs in the natural gas, the court said:

> Without the consent of the owner of the land, the public cannot appropriate it, use it, or enjoy any benefit whatever from it. This power of the owner of the land to exclude the public from its use and enjoyment plainly distinguishes it from all other things with which it has been compared, in the use, enjoyment and control of which the public has the right to participate, and tends to impress upon it, even when in the ground in its natural state, at least, in a qualified degree, one of the characteristics or attributes of private property.[32]

Under this theory the owner of the land can have no "title" to the oil and gas in place, but he does have the exclusive right to drill and produce from his own tract and to become the owner of the product when it is brought up to the surface. It is sometimes said that his right consists of the privilege, enjoyed by all who own the superincumbent lands, to take the oil and gas from the common source of supply by wells on his own land.[33]

In qualified ownership states oil and gas interests are not the subject of sale apart from the surface in the sense that title to them is regarded as passing. On the other hand, an instrument purporting to grant or except these substances has the effect of conveying or excepting the right to enter upon the land for the purpose of drilling for oil and gas and reducing them to possession, at which time the title is said to become perfect.[34] The practical effect is similar to the severance of minerals from the surface in ownership jurisdictions.

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[31] 155 Ind. 461, 57 N.E. 915 (1900).

[32] *Id.* at 469, 57 N.E. at 915.

[33] Ohio Oil Co. v. Indiana, 177 U.S. 190 (1900).

[34] Barker v. Campbell-Ratcliff Land Co., 64 Okla. 249, 167 Pac. 468 (1917).

OHIO: ABSOLUTE, QUALIFIED, OR NEITHER

Several writers have classified Ohio as an absolute ownership state on the basis of expressions found in *Kelley v. Ohio Oil Co.*, and two later cases.[35] Actually, the *Kelley* case contains language which would support either theory. The court said: "Petroleum oil is a mineral, and while in the earth it is part of the realty, and should it move from place to place by percolation or otherwise, it forms part of that tract of land in which it tarries for the time being. . . ." The court, however, then said that when oil is brought to the surface "then for the first time it becomes the subject of distinct ownership separate from the realty, and becomes personal property, the property of the person into whose well it came." [36] In *Pure Oil Co. v. Kindall* [37] the Ohio court clearly adopted the ownership theory. It quoted with approval the following statement describing the absolute ownership concept: " 'By such grant or reservation there is created a separate and distinct corporeal interest, or estate, in the land, which is capable of ownership to the same extent and in the same manner as the surface.' " [38] There are expressions which would lead to the opposite conclusion in the more recent case of *Back v. Ohio Fuel Gas Co.*[39] In that case the question was whether an instrument in the form of a general warranty deed purporting to convey the oil and gas together with surface easements was properly recorded in the lease and license records rather than the deed records. The court gave an affirmative answer and held that the record gave constructive notice to a subsequent purchaser. The court looked to the language of the particular instrument and concluded that it was the intention of the parties that it should convey no more than a license to operate for oil and gas. One reason was that the habendum clause and the covenants for title referred to oil and gas rather than to oil and gas in place. Nevertheless there is language indicating that it would be impossible to create a separate corporeal estate in the oil and gas. The court said: "As a matter of fact, many authorities hold that the owner of the land surface does not own any oil or gas which may be 'in place' thereunder." The court quoted from an encyclopedia the statement: "that the landowner's only right is to extract them, and that he has no title to them until he does so." [40] The *Kelley* case was cited in support of this view, and the *Kindall* case was not mentioned. The question,

[35] Pure Oil Co. v. Kindall, 116 Ohio St. 188, 156 N.E. 119 (1927); Fourth Trust Co. v. Wolley, 31 Ohio App. 259, 165 N.E. 742 (1928).

[36] Kelley v. Ohio Oil Co., *supra* note 9, at 328, 49 N.E. at 401.

[37] 116 Ohio St. 188, 156 N.E. 119 (1927).

[38] *Id.* at 202, 156 N.E. at 123.

[39] 160 Ohio St. 81, 113 N.E.2d 865 (1953).

[40] *Id.* at 86-87, 113 N.E.2d at 868.

therefore, is not settled in Ohio and the way is open for the adoption of either view.

Protection Against Trespass

When the cases are examined, few substantive differences result from the adoption of one theory of ownership as opposed to the other. Whatever the theory of ownership, the doctrine, "so use your property as not to injure the land of another," applies. In a title theory state an operator has been held liable to adjacent landowners for injuries to the reservoir and for oil and gas drained away and wasted as a result of negligent operations.[41] There are similar holdings in the qualified ownership states. Thus in *McCoy v. Arkansas Natural Gas Co.*[42] it was held that a complaint charging defendant with negligent operation resulting in a blowout on defendant's land stated a cause of action. It seems that a different measure of damages may result from the opposing theories of ownership. In the *McCoy* case, the court concluded that while the plaintiff had no claim for gas which had been drained from his property, he would be entitled to recover the amount by which the value of the mineral rights on his land had been reduced by the act of negligence.[43] In Texas, an absolute ownership state, the value of oil and gas wrongfully drained has been used as the criterion for determining damage.[44] Courts in the qualified ownership jurisdictions have not hesitated to grant injunctive relief at the instance of one of the owners in a reservoir to prevent wasteful dissipation of the common source of supply even though the plaintiff does not "own" the gas or oil.[45]

In both types of jurisdictions, the owner of the minerals in land is protected against trespass. Since such an owner has the exclusive right to drill and produce from his own land, it follows that the unauthorized drilling and production by a stranger is a trespass in either jurisdiction. While there are minor variations in the measure of damages in several states, these differences seem to depend in no way on the theory of ownership followed.[46] In both types of state, an operator who by directional drilling bottoms his well on a neighboring tract—the "slant well"—is liable in trespass. This is so far true that in California, where the qualified ownership theory is

[41] Elliff v. Texon Drilling Co., 146 Tex. 575, 210 S.W.2d 558 (1948), 62 Harv. L. Rev. 146 (1948), 27 Texas L. Rev. 349 (1949).

[42] 184 La. 102, 165 So. 632 (1936).

[43] See Louisville Gas Co. v. Kentucky Heating Co., 132 Ky. 435, 111 S.W. 374 (1908), for a similar damage computation.

[44] Texon Drilling Co. v. Elliff, 216 S.W.2d 824 (Tex. Civ. App. 1948).

[45] Manufacturers' Gas & Oil Co. v. Indiana Natural Gas & Oil Co., *supra* note 31; Louisville Gas Co. v. Kentucky Heating Co., 117 Ky. 71, 77 S.W. 368 (1903).

[46] 1 Kuntz, Oil and Gas § 11.3 (1962); 1 Williams and Meyers, Oil and Gas Law §§ 225-29 (1964).

established, a defendant was held liable for the gross value of the oil produced from an intentionally deviated well without any allowance for production costs.[47]

Exercise of Police Power for Conservation

Since oil and gas are irreplaceable, valuable natural resources, it is now well settled that the state has inherent power to prevent their waste through exercise of the police power; nevertheless, the more cautious states look to express constitutional support for the power.[48] It is settled that this power to regulate is not dependent upon the theory of ownership followed.[49] It will be recalled that the Rule of Capture was justified on the ground that each owner of land could protect himself from drainage by self-help. This remedy has been rendered largely ineffective by conservation statutes. As a result, a state legislature may provide for regulation of drilling and production to protect the correlative rights of such an owner. Indeed, it is under a duty to protect such rights when regulating to prevent waste, so that each owner will have a reasonable opportunity to produce his fair share.[50]

The foregoing discussion demonstrates that there is no significant difference between the ownership and qualified ownership states insofar as substantive rights are concerned. While certain procedural differences flow from subclassifications, such differences depend in part on the theory of ownership which is adopted. Before passing to these, however, it might be well to attempt to describe in a more meaningful way the character of the property rights which a landowner has in the oil and gas beneath his tract. To this writer the most descriptive answer is found in the conservation cases. The statutes and cases of all jurisdictions recognize that the property right of an owner of oil and gas which is subject to the protection of due process and equal protection clauses of the Constitution is the right to a reasonable opportunity to produce or receive his fair share of the oil and gas.[51] Stated differently, the substantive right is

[47] Alphonzo E. Bell Corp. v. Bell View Oil Syndicate, 24 Cal. App. 2d 587, 76 P.2d 167 (1938).

[48] Ohio Const. art II, § 36; Tex. Const. art. 16, § 59(a).

[49] See the discussions in Henderson Co. v. Thompson, 300 U.S. 258 (1937); F. C. Henderson, Inc. v. Railroad Comm'n, 56 F.2d 218, 221 (W.D. Tex. 1932); Walker, *supra* note 14.

[50] Ohio Oil Co. v. Indiana, *supra* note 33. See also Corzelius v. Harrell, 143 Tex. 509, 186 S.W.2d (1945), 24 Texas L. Rev. 97 (1946). A brief discussion is found in A.B.A. Section on Mineral Law, "Conservation of Oil and Gas—A Legal History—1948," 497-99 (1949).

[51] Hardwicke & Woodward, "Fair Share and the Small Tract in Texas," 41 Texas L. Rev. 75 (1962); Woodward, "The Fair Share Rule," V Interstate Oil Compact Comm'n Bulletin 31 (June, 1963).

the assurance of a chance to produce the recoverable oil and gas in place beneath his land. The uniformity of the various states in this respect supports the proposition that the divergent theories of ownership are in fact little more than attempts to describe a single concept in different language.[52]

The right of surface use should be mentioned here. Frequently there is a complete severance of the minerals from the surface, so that the owner of one of the estates has no interest in the other. Mineral grants and exceptions sometimes contain express provisions with respect to the use of the surface by the mineral owner, while in other instances, the instruments are silent on this subject. This is particularly true of deeds executed some years ago. When this is the case, the mineral owner obtains by implication the right to use so much of the surface as is reasonably necessary for the enjoyment of the mineral estate.[53] This is true irrespective of the theory of ownership adopted.[54]

Classification of Interests as Corporeal or Incorporeal

It is necessary at this point to draw a distinction between mineral and royalty interests. The owner of the mineral estate, as distinguished from a royalty interest, has the power to drill and produce and to confer this right upon others.[55] Development normally occurs through the execution of a lease by the mineral owner. While in most states the owner of an undivided interest in minerals may execute a lease which will empower the lessee to develop,[56] it is essential to have joinder of all such owners if their interests are

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[52] See 1 Kuntz, *op. cit. supra* note 15, § 3.1.

[53] Melton v. Sneed, 188 Okla. 388, 109 P.2d 509 (1940); Warren Petroleum Corp. v. Monzingo, 157 Tex. 479, 304 S.W.2d 362 (1957); Cassin, "Land Uses Permitted an Oil and Gas Lessee," 37 Texas L. Rev. 889 (1959); Keeton & Jones, "Tort Liability and the Oil and Gas Industry," 35 Texas L. Rev. 1 (1956); McMahon, "Rights and Liabilities With Respect to Surface Usage By Mineral Lessees," Sixth Annual Institute on Oil and Gas Law and Taxation 231 (1955).

[54] See 1 Williams & Meyers, *op. cit. supra* note 17, § 218, for a detailed discussion of the right of surface use. See also 1A Summers, Oil and Gas § 133 (perm. ed. 1954).

[55] This refers to a mineral interest in traditional form. In recent years the so-called "non-executive mineral interest" has gained considerable popularity. It is created by a grant or reservation of a fractional interest in the minerals, but the exclusive right to execute leases is expressly given to one of the parties to the exclusion of the other. The holder of such an interest would, of course, have no right to participate in the execution of leases. See, *e.g.*, Pan Am. Petroleum Corp. v. Cain, 163 Tex. 323, 335 S.W.2d 506 (1962), 41 Texas L. Rev. 326; De Busk v. Cosden Petroleum Corp., 262 S.W.2d 767 (Tex. Civ. App. 1953).

[56] Annot., 91 A.L.R. 205 (1934); Annot., 40 A.L.R. 1400 (1926).

to be bound by the lease.[57] In states following the ownership theory it is possible for the owner of land to sever the minerals from the surface by a grant which will confer upon the grantee a corporeal or possessory estate in the minerals.[58] Similarly, it is possible for a person who owns land, or the minerals therein, to confer upon his lessee a corporeal interest in the minerals. In Texas, for example, an ordinary lease creates in the lessee a corporeal or possessory estate in the oil and gas. This is true irrespective of normal variations in the granting clause, that is, whether it purports to "lease, let and demise" or to "grant, sell and convey." [59] However, in some of the other ownership states the lease creates in the lessee only an incorporeal interest. The Kansas and Arkansas courts have taken this view.[60] In Pennsylvania much importance has been attached to the wording of the particular granting clause in determining whether the interest of the lessee is corporeal or incorporeal.[61] It would appear to be impossible, in common law logic, for the lessee to obtain a corporeal estate in the oil and gas in a qualified ownership jurisdiction. In nearly all of the qualified ownership states where the question has arisen, it has been held that the lessee obtains an incorporeal interest in the nature of a profit a prendre.[62]

The owner of a royalty interest has no right to drill nor produce.[63] Similarly, he has no power to confer this right upon others. It follows, therefore, that his joinder in the lease is not necessary in order to bind his interest.[64] The courts have not often had occasion to consider the subject, but it seems clear that a royalty

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[57] Annot., 5 A.L.R.2d 1368 (1949). On co-tenancy problems in general, see 2 Williams & Meyers, Oil and Gas Law §§ 502-10 (1964).

[58] See, *e.g.*, Humphreys-Mexia Co. v. Gammon, 113 Tex. 247, 254 S.W. 296 (1923).

[59] Stephens County v. Mid-Kansas Oil & Gas Co., 113 Tex. 160, 254 S.W. 290 (1923); Walker, "The Nature of the Interest Created by an Oil and Gas Lease in Texas," 7 Texas L. Rev. 539 (1929).

[60] Standard Oil Co. v. Oil Well Salvage Co., 170 Ark. 729, 281 S.W. 360 (1926); Burden v. Gypsy Oil Co., 141 Kan. 147, 40 P.2d 463 (1935).

[61] Barnsdall v. Bradford Gas Co., 225 Pa. 338, 74 Atl. 207 (1909); 1A Summers, Oil and Gas § 155 (perm. ed. 1954).

[62] Heller v. Dailey, 28 Ind. App. 555, 63 N.E. 490 (1902); Rich v. Doneghey, 71 Okla. 204, 177 Pac. 86 (1918). A recent survey of the cases is found in 1 Williams & Meyers, Oil and Gas Law § 209 (1964).

[63] Greenshields v. Warren Petroleum Corp., 248 F.2d 61 (10th Cir. 1957); Stokes v. Tutvet, 134 Mont. 250, 328 P.2d 1096 (1958); Sullivan, Oil and Gas Law § 118 (1955).

[64] Federal Land Bank v Nicholson, 207 Okla. 512, 251 P.2d 490 (1952); Schlittler v. Smith, 128 Tex. 628, 101 S.W.2d 543 (1937)

interest should be classified as an incorporeal interest similar to the right to receive unaccrued rent.[65]

It is generally accurate to say that little difference is likely to occur in the final solution of cases from the classification of an interest as possessory or nonpossessory. There have been a few cases in which the distinction has made an important difference, and there are some possibilities which have apparently not yet been litigated. The classification of an interest as corporeal or incorporeal may have an effect on the right to obtain partition of an undivided interest in some states. In Texas, for example, the owner of a corporeal interest created by an oil and gas lease has a statutory right to partition.[66] The owner of a royalty interest which is nonpossessory can neither compel nor defeat a partition.[67] In *Pasture v. Niswanger*[68] the Arkansas court held that the owner of a fractional interest in a leasehold estate was not entitled to partition because the lease was not regarded as passing title to the oil and gas in place.[69] Classification of an interest as corporeal or incorporeal has also been the determinative factor in deciding whether the holder of the interest was entitled to bring a possessory action in some states. Thus in Texas, a lessee is permitted to bring the statutory action for possession because his estate is possessory in nature.[70] The owner of a royalty interest is not.[71] This does not mean that the owner of an incorporeal interest is without a remedy, but merely that the form of the remedy is different.

A difference could arise out of the common law rule that the owner of an incorporeal interest can lose it by abandonment, since such a loss is impossible in the case of a corporeal interest. No case has been found in which a royalty interest has been lost by abandonment; no doubt for the reason that it would usually be impossible to establish the necessary element of intent. In Texas an oil and gas lessee may lose his interest through non-use by what has been

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65 A majority of the cases seem to take this view. 3A Summers, Oil and Gas §§ 572-85 (perm. ed. 1958); Annot., 131 A.L.R. 1371 (1941); Annot., 90 A.L.R. 770 (1934).

66 McKee v. McKee, 12 S.W.2d 849 (Tex. Civ. App. 1928).

67 Douglas v. Butcher, 272 S.W.2d 553 (Tex. Civ. App. 1954); Chaffin v. Hall, 210 S.W.2d 191 (Tex. Civ. App. 1948).

68 226 Ark. 486, 290 S.W.2d 852 (1956).

69 *Accord,* Gulf Ref. Co. v Hayne, 138 La. 555, 70 So. 509 (1915).

70 Standard Oil Co. v. Marshall, 265 F.2d 46 (5th Cir. 1959). See Barnsdall v. Bradford Gas Co., 225 Penn. 338, 74 Atl. 207 (1909) (lessee able to maintain the action of ejectment).

71 Grasty v. Wood, 230 S.W.2d 568 (Tex. Civ. App. 1950).

sometimes called "abandonment," but which has been explained as an implied special limitation of non-use for any of the purposes for which the lease was granted.[72] Insofar as the lessee's interest is concerned, it seems unlikely that the question can arise under the modern lease forms in common use.

Theoretically, there would be a difference as to the application of the adverse possession statutes to the acquisition or loss of a severed mineral interest, depending upon its classification as corporeal or incorporeal. If the interest is possessory, then the ordinary land limitation statutes would apply.[73] If the interest is incorporeal, it could be acquired or lost by prescription, but the adverse possession statutes as such would have no application. It appears, however, that the cases reveal no difference in result.[74]

Classification of Interests in Minerals as Real or Personal Property

It seems to be true in all jurisdictions that a severed mineral interest and also the lessee's interest under an oil and gas lease are interests in land.[75] Though there are occasional expressions to the contrary, it seems that royalty interests and also most of the interests carved out of the lessee's estate are similarly regarded. There exists, however, no uniformity as to whether such interests are to be treated as real or personal property. The traditional common law basis for this classification is determined by the duration of the estate.[76] If the interest is for life, or has a possibility of enduring perpetually, it is freehold in character and hence classified as real property. Interests in land which are less than freehold, such as an estate for a term of years, are labeled as personal property and chattels real by this traditional view. In some jurisdictions long-term leases—typically for more than one year—are now regarded as creating real property interests because of the interpretation placed on statutes dealing with conveyancing, descent and distribution, and real estate broker's commissions.[77]

In most states grants or reservations of mineral interests may be perpetual in duration. Under the Louisiana Civil Code, however,

[72] Texas Co. v. Davis, 113 Tex. 321, 254 S.W. 304, *motion for rehearing denied*, 255 S.W. 601 (1923). See Walker, "The Nature of the Property Interests Created by an Oil and Gas Lease in Texas," 8 Texas L. Rev. 483, 493-511 (1930).

[73] See, *e.g.*, Houston Oil Co. v. Moss, 155 Tex. 157, 284 S.W.2d 131 (1955).

[74] 1 Williams & Meyers, Oil and Gas Law § 210.7 (1964).

[75] Walker, "The Nature of the Property Interests Created by an Oil and Gas Lease in Texas," 7 Texas L. Rev. 539, 563 (1929).

[76] 2 Powell, Real Property § 222 (1950).

[77] *Ibid.* See Abraham v. Fioramonte, 158 Ohio St. 213, 107 N.E.2d 321 (1952).

the right to conduct mineral operations cannot endure for a period of more than ten years unless the right is exercised by the commencement of such operations within that period.[78] A ten-year liberative prescription is also applicable to a royalty interest created by a grant or reservation in Louisiana.[79] A similar statute was enacted in Tennessee in 1939.[80] Apart from these two states, severed mineral and royalty interests may be, and frequently are, perpetual in duration. In recent years it has been common practice to create what is known as term mineral or royalty interests. These are usually for a fixed number of years and so long thereafter as oil, gas, or other minerals may be produced. Less common are mineral or royalty interests created for a fixed term of years. Only the latter would be regarded as personal property by the accepted common-law test.

Modern oil and gas leases are nearly always for a fixed term of years "and so long thereafter as oil, gas or other minerals may be produced." Some of the older lease forms provided for a fixed number of years. In most of the jurisdictions following the absolute ownership theory, an oil and gas lease in the ordinary modern form is regarded as giving the lessee an interest in land which is classified as real estate.[81] In Kansas, for reasons not entirely clear, the lessee's interest has been classified as personal property for most purposes. Apparently the Kansas courts have taken the view that because the lessee's interest is regarded as incorporeal, it necessarily follows that it should be classified as personal property.[82] It is difficult to make any generalization about the qualified ownership jurisdictions. In classifying the lessee's interest as real or personal property, the California courts have used the traditional criterion of duration of the estate. Thus, in *Dabney v. Edwards*[83] it was held that a lease for a fixed term of years created an interest which was to be classified as personal property, while a lease in the modern form with a fixed primary term and a "so long thereafter" clause was freehold in duration and therefore real estate.[84] However, an Oklahoma case

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78 Wemple v. Nabors Oil & Gas Co., 154 La. 483, 97 So. 666 (1923).

79 St. Martin Land Co. v. Pinckney, 212 La. 605, 33 So. 2d 169 (1947); Vincent v. Bullock, 192 La. 1, 187 So. 35 (1939).

80 Tenn. Code Ann. § 64-704 (1955). See also Va. Code Ann. §§ 55-154 (1964), 55-155 (1956).

81 Stokeley v. State, 149 Miss. 435, 115 So. 563 (1928); Terry v. Humphreys 27 N.M. 564, 203 Pac. 539 (1922); Stephens County v. Mid Kansas Oil & Gas Co., *supra* note 59.

82 Burden v. Gypsy Oil Co., *supra* note 60.

83 5 Cal. 2d 1, 53 P.2d 962 (1935).

84 See 1A Summers, Oil and Gas Law §§ 155-70 (perm. ed. 1954), for a discussion of the cases in the various states.

held that the lessee's interest is personal property, irrespective of the duration of the lease.[85] The difficulties which can arise from the classification of the lessee's interest as personal property are demonstrated in *Continental Supply Co. v. Marshall*,[86] an Oklahoma diversity case, in which the court reviews a number of the Oklahoma cases. The court noted that an oil and gas lease is neither a conveyance of real estate within the meaning of the statutes governing sales by personal representatives, within the judgment lien statutes, nor within the ad valorem tax statutes. On the other hand, it is a conveyance of real estate within the meaning of the Statute of Frauds, the statute relating to formalities of conveyances by corporations, the laws relating to conveyances of the homestead, the recording statutes, and the statute fixing the measure of damages for breach of title covenants.

Royalty interests are classified in some states as real estate if they are freehold in duration.[87] In Kansas a royalty interest is classified as personal property irrespective of its duration.[88] This is apparently because a conveyance of such an interest is regarded as a mere contract to share oil and gas after it has been brought to the surface, and not a transfer of a present interest in the land. An Ohio Supreme Court decision contains this dictum: "Royalty is personal property, and is not realty." [89] In an earlier case the same court held that an oral contract modifying the royalty provisions of an oil and gas lease was not within the Statute of Frauds.[90] One basis for the decision was that royalty was personal property, but the court discussed authorities indicating that it could have reached the same result on other grounds. While the little authority found indicates that a royalty interest will be treated as a chattel real in Ohio, further consideration of the question is apparently not foreclosed.

As indicated by the foregoing discussion, the classification of a particular interest as real or personal property has been found to be of significance mainly in connection with the interpretation of statutes which use the general terms "real property" or "personal property" without any specific reference to oil and gas. The problem

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85 State v. Shamblin, 185 Okla. 126, 90 P.2d 1053 (1939) (interest not subject to ad valorem taxation).

86 152 F.2d 300 (10th Cir. 1945).

87 Arrington v. United Royalty Co., 188 Ark. 270, 65 S.W.2d 36, (1933); Kentucky Bank & Trust Co. v. Ashland Oil Co., 310 S.W.2d 287 (Ky. Ct. App. 1958); Mullins v. Evans, 43 Tenn. App. 330, 308 S.W.2d 494 (1957); Sheffield v. Hogg, 124 Tex. 290, 77 S.W.2d 1021 (1934).

88 Lathrop v. Eyestone, 170 Kan. 419, 227 P.2d 136 (1951).

89 Pure Oil Co. v. Kindall, 116 Ohio St. 188,, 156 N.E. 119 (1927).

90 Nonamaker v. Amos, 73 Ohio St. 163, 76 N.E. 949 (1905).

has most frequently arisen with respect to tax statutes.[91] One notes that the escape from taxation of any oil and gas interest is likely to be brief since legislatures generally respond promptly to any decision exempting such interests.[92] The right to statutory partition may depend upon whether the interest is classified as real or personal property. Thus a Kansas court held that the owner of a lease on an individed interest in the minerals was not entitled to partition because the statutes applied to partition of real property only.[93] Other instances are found in statutes relating to the commissions of real estate brokers,[94] formalities of conveyancing,[95] and the recording and foreclosure of mortgages on oil and gas interests.[96]

Whatever may be said for the flexibility which necessarily results from classifying particular oil and gas interests as personal property, it is believed that the need for certainty, especially as to formalities of conveyancing and to recording, is as important as for those interests which are everywhere conceded to be real estate. This certainty, and the resulting security of titles, can best be achieved by treating all oil and gas interests as real property.

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[91] State v. Shamblin, *supra* note 85; Annot., 59 A.L.R. 701 (1929); See Sheffield v. Hogg, *supra* note 87; Stephens County v. Mid-Kansas Oil & Gas Co., *supra* note 59; Annot., 59 A.L.R. 701 (1929).

[92] 1 Williams & Meyers, Oil and Gas Law § 213.3 (1964).

[93] Beardsley v. Kansas Natural Gas Co., 78 Kan. 571, 96 Pac. 859 (1908).

[94] Dabney v. Edwards, *supra* note 83.

[95] Terry v. Humphreys, *supra* note 81.

[96] Continental Supply Co. v. Marshall, *supra* note 86. See Vagts, "The Impact of the Uniform Commercial Code on the Oil and Gas Mortgage," 43 Texas L. Rev. 825 (1965), for a discussion of the Uniform Commercial Code on security interests in oil and gas.